STATEMENT OF

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Madam Chairman and Members of the Subcommittee, I appreciate the opportunity to testify today on the Fiscal Year (FY) 2003 budget request for the Minerals Management Service (MMS). We have looked closely at our ongoing operations and responsibilities and this request reflects our best assessment of the funds needed to carry out critical MMS programs during FY 2003.

The MMS is requesting $281.0 million, including $10.4 million for a government-wide legislative proposal to shift to agencies the full cost of the CSRS pension system and the Federal employee health benefits program for current CSRS employees. Without the legislative proposal, the request is $270.6 million, a net increase of $ 11.1 million above the 2002 enacted level, and includes both programmatic and uncontrollable cost increases.

Our budget request is based upon our accomplishments in successfully implementing and completing past budget initiatives. It is also based upon the challenges confronting us during the next fiscal year and beyond, which are the reasons for the increases in budgetary requirements. The request includes funding to:

· manage the increased workload and complicated industry requirements for drilling and production-related activities in the Gulf of Mexico Region,

· provide additional resources to keep pace with the increased demand on our revenue management network and enterprise systems,

· acquire an automated liquids (oil) management system to support the pilot royalty-in-kind programs, and

· begin a five year e-government initiative that will deliver web-based, paperless transactions and better manage data, resulting in reduced future costs and improved information delivery to citizens.

The MMS manages the nation's oil, natural gas, and other mineral resources on the Outer Continental Shelf (OCS), and collects, accounts for, and disburses revenues from offshore federal mineral leases and from onshore mineral leases on Federal and American Indian lands. To carry out this mission, MMS manages two very important programs - the Offshore Minerals Management (OMM) Program and the Minerals Revenue Management (MRM) Program. These programs provide major economic and energy benefits to the Nation, taxpayers, states and the American Indian community.

The MMS has leased and currently manages more then 40 million acres of the OCS. More than 13.1 billion

barrels of oil and 146.4 trillion cubic feet (tcf) of natural gas have been produced from the OCS since 1953.

From an economic standpoint, MMS will account for a projected $4.2 billion in Federal receipts in FY 2003. MMS will also account for an additional $200 million in receipts for American Indian tribes and individual American Indian owners, and $39 million in shared mineral revenue receipts with coastal states. The Federal receipts include $2.8 billion from OCS receipts and $1.4 billion from onshore receipts. From a taxpayer's perspective, that converts to:

· $1.9 billion deposited to the General Fund of the U.S. Treasury;

· $674 million in mineral revenue payments made to onshore states;

· $897 million transferred to the Land and Water Conservation Fund;

· $536 million credited to the Reclamation Fund; and

· $150 million for the Historic Preservation Fund.

The receipts I have described above are derived from the accomplishment of the Bureau's two program missions. MMS has recently celebrated its 20th anniversary, and during this relatively short time these two programs have experienced dramatic and profound changes in the business, energy and government climates in which they operate. These changes have challenged MMS to keep pace, and I believe that the bureau has risen to the challenge. I would now like to review a few of MMS's recent achievements and what MMS sees as its challenges for the future.

OMM Program Achievements

OCS and the Nation's Energy Supply

The OCS continues to play a critical role in supplying the nation's energy needs. It is estimated that oil and gas production from the OCS will account for over 25 percent of the country's total production in FY 2003. The average combined shallow and deepwater production in 2003 is estimated to be about 587 million barrels of oil and 5.1 tcf of gas.

Record Setting Activity in the Gulf of Mexico (GOM)

Drilling in the GOM deep water has increased dramatically over the last decade. Today, deepwater drilling continues to be at an all time high with over 45 rigs drilling in water depths of over 1,000 feet, compared to just nine in 1990. The number of wells drilled in a single year in water depths greater than 200 meters reached a record high of 302 in 2001, and a record 1,408 well starts were drilled in the GOM last fiscal year. This is a 52% increase from the 928 well starts drilled in FY 1995.

Safety remains a top priority.

The MMS regards the safety of personnel, the environment, and operations as top priorities. Prevention is our most important safety strategy. The continued movement of industry into deeper waters and the overall increased industry activity in the GOM have increased both the level and complexity of monitoring and ensuring safe OCS operations. Likewise, there has been a significant rise in the number of operators on the

OCS, some without the same level of experience as the more seasoned operators.

MMS continues to work with industry and other agencies to ensure the continued safety of offshore operations. In 2002, the MMS will be authorized to inspect and enforce U.S. Coast Guard safety regulations on fixed OCS platforms. By authorizing MMS to also check for compliance with Coast Guard safety regulations, we avoid duplicating functions, reduce Federal costs, and increase the frequency of these critical safety inspections.

OMM Program Challenges

Meeting Future National Energy Needs

The U.S. is the most mature petroleum-producing region in the world. Much of the Nation's easily located oil and gas has already been extracted. Despite this, domestic discoveries and reserve additions over the past decade have replaced 100 percent of the natural gas and 79 percent of the crude oil produced during this period. Advanced technologies have allowed economical access to domestic resources that are concentrated in deeper formations, tighter zones, deeper water, more sensitive environments, and increasingly more unconventional settings. In 1998, the U.S. Department of Energy (DOE) estimated that two-thirds of the 603 billion barrels of known oil reserves in the U.S. remained untapped.

While new sources of energy may be on the horizon, oil and gas will continue to be important during the next 20 to 30 years, and the DOE estimates that dependence on oil and gas will increase significantly during that time. Because of this dependence, MMS programs are vitally important to the security of the Nation and the well being of the national economy. One such example is our royalty-in-kind program that will enable MMS to meet the President's November 2001 directive to fill the Strategic Petroleum Reserve.

Demand for oil and gas uncharacteristically declined in 2001. This is attributed mainly to the decline in air travel after September 11th and an unseasonably warm winter. Nevertheless, demand for oil is expected to increase once again in 2002. By 2003, DOE projects annual average petroleum demand to exceed 20 million barrels per day for the first time.

While oil production on the OCS is projected to increase through 2010, the long-term overall U.S. oil production is projected to decline. This decline is projected at an average annual rate of 0.7 percent between 1999 and 2020, to 5.1 million barrels per day. The share of U.S. oil demand met by net imports is projected to increase from 56 percent in 1999 to 70 percent in 2020, an average annual increase of 2.5 percent

U.S. demand for natural gas is projected to increase from 22 tcf in 1998 to as high as 29 tcf by the year 2010 and 31.3 tcf by 2015. This is a 50 percent increase over what the Nation consumes today. If the OCS is expected to maintain the same percentage contribution towards future U.S. gas consumption, the annual gas production from federal waters will have to increase 7 to 8 tcf. Natural gas is clearly the fuel of choice for the Nation's future energy use because it is a cleaner burning fuel.

Safety and Environmental Protection

While development of offshore mineral resources has already meant billions of dollars in revenues to the United States, MMS is responsible for ensuring that those economic benefits are not made at the expense of safe operations and environmentally responsible development. The move into deeper water and the overall rise in activity have increased both the level and complexity of monitoring OCS operations. The number of

operators drilling in the GOM has increased over the past several years by about 30 percent. Some of these new operators are not as experienced as those that have been working in the GOM for a longer time. There is also a much greater reliance by all operators on the use of contractors. In addition, the offshore industry downsized significantly throughout the 1980s and 1990s. All of these events have reduced the pool of skilled offshore workers. The presence of workers with a minimum of offshore experience is placing an added burden on the inspection and compliance program.

One of MMS's top priorities is ensuring that industry maintains its excellent safety and environmental record as the level of activity increases in both amount and complexity. From a safety perspective, recent statistics indicate that the rate of injuries and illnesses for offshore workers is less than half the rate for the private sector as a whole. On the environmental front, since 1985, over 63 billion barrels of oil have been produced from the OCS with only 0.001% spilled. Natural seeps contribute more than 150 times this amount to the marine environment. Maintaining the OCS's good safety and environmental record is critical to preserving the public's confidence in the integrity of the program and to facilitating further OCS production. If a serious incident were to occur and we were prohibited from further development of these promising areas, the Nation would lose the significant contributions that the Offshore Program makes to the economy in the form of revenues and secure supplies of oil and natural gas.

Deepwater Production

Production from deepwater wells continues to increase as compared to prior years. In 1985, for example, only six percent of the GOM's oil production came from deepwater wells as compared to over 50 percent in FY 2001. Natural gas production from deepwater areas in the GOM increased from less than 1 percent of total gas production in 1985 to over 20 percent in FY 2001. As discussed earlier, drilling activities continue to reach record highs in the GOM.

The continuing increase in production and drilling activities in the GOM places additional workload demands on MMS in the areas of environmental assessments, field determinations, engineering, inspection, and production and deepwater operation plan reviews.

Maintaining a Viable OCS Program

One of the agency's core responsibilities in managing OCS leasing and development is to ensure that our leasing decisions fully consider the possible risks to coastal communities and environments of offshore development**,** and that our regulatory efforts ensure the highest degree of safety and protection possible in day-to-day operations.

The MMS is entering the final stages in the development of its next OCS 5-Year Program covering the 2002-2007 timeframe. The comment period on the Proposed Program and the draft environmental impact statement closed in January 2002. A final EIS will be prepared and a proposed final program will be submitted to the President and Congress in April 2002. Following a 60-day waiting period, the Secretary is scheduled to approve the new program in June with an effective date of July 1, 2002.

Expanding Electronic Government

Since the oil and gas resources of the OCS, though abundant, are ultimately exhaustible, MMS must manage these resources in the most prudent manner possible. To do this, MMS must impose complex requests and reporting requirements on the oil and gas industry. It must also share information, analysis, and databases

with other government and public entities. Together, these management responsibilities create intense pressure for automation of many recurring processes. To fulfill each of its mandated tasks, MMS must facilitate the exchange of OCS-related information within a complex network of stakeholders (industry, other agencies, states, the public). That fact is the basis of OMM's e-Government vision.

OMM's e-Government framework consists of investment in core infrastructure, such as a regulatory data model, redesigned web-enabled corporate database, document management, security, and a data warehouse to support its business functions. A strong OMM infrastructure will support web-based, customer-responsive solutions; facilitate internal analysis; and set a foundation for future integrated systems. Additional investments will support processes such as permitting, inspections, Freedom of Information Act, public commenting, and industry reporting. To ensure that the foundation is flexible, capabilities will be built in a coordinated and modular fashion, using commercial off-the-shelf applications and outsourcing when feasible. MMS's approach is driven by customers and stakeholders, focused on mission and strategy, process-efficient, and technology-enabled.

MMS will also work closely with the Bureau of Land Management to ensure data exchange compatibility with future onshore oil and gas program applications.

FY 2003 Budgetary Impact

To address these challenges, we are requesting $5.0 million to accommodate the increased demand for services in the GOM region, and $8.7 million as first-year funding for development of OMM's E-government initiative.

Minerals Revenue Management Program Achievements

Reengineered program, processes, and systems

FY 2002 brought the culmination of many fundamental changes that were presented in the *Roadmap to the Future* published in November 1998. In FY 2001, the MRM realigned its organizational structures and resources to support the reengineered business processes that will yield the significant and recurring benefits sought from the royalty reengineering initiative. In its realignment MRM also changed its name from Royalty Management Program to better reflect the program's mission. The new MRM organizational structures were developed based on extensive input from employees and in close consultation with industry, State, and tribal partners.

In FY 2002, MRM implemented a new systems infrastructure to support our reengineered business processes. These fundamental changes to organizations, infrastructures, and processes require significant new skill sets, bringing opportunities to build knowledge of new systems, understand relationships, develop expertise, and refine processes. The two reengineered end-to-end business processes support the continued emphasis on our Indian trust responsibilities as well as help us achieve our stretch goals.

· The Financial Management Process manages the information and money that flows through the MMS to program beneficiaries. The new process shortens the receipt and distribution cycle, providing beneficiaries with access to their funds sooner.

· The Compliance and Asset Management Process ensures that all revenues, whether received through in-kind or in-value royalties, are paid timely and accurately. This process introduces fundamental change to the

way MMS has historically done compliance work. Instead of focusing on payors in evaluating royalty payments, the MRM now focuses on properties and producing areas. This new process introduces a significant reduction in business cycle time, with a goal of completing all compliance work, including audit, within 3 years or less after the payment was made. With the property and producing area focus, this process also well positions the MRM to support its royalty in-kind asset management strategies.

Consummate Asset Manager

The asset management concepts developed through reengineering and demonstrated by the RIK pilots and operational model support MRM's mission to be "the best in the business", pursuing fair market value and cost-effective collection and disbursement of royalties whether collected in-kind or in-value. MMS is currently focusing its development of the RIK asset management strategy in the Gulf of Mexico. At present, about 84 percent of the Federal oil and gas revenues are produced from leases on the Outer Continental Shelf. Most of these revenues come from the Gulf of Mexico, which offers the following asset management advantages:

· Close proximity to market centers

· Access to extensive systems for the delivery of mineral production to buyers

· Relatively few lease contracts to administer

In FY 2002, MMS began the development of the automated infrastructure to support the gas RIK program. When complete, this development effort will provide the needed tools to support gas RIK business processes. MMS expects to complete implementation of the RIK gas automated infrastructure in early FY 2003.

Indian Trust Responsibilities

In accordance with the Department's American Indian trust responsibilities, MMS has a special dedication to the tribes and individual American Indian mineral owners. MMS serves American Indian tribes and individual American Indian mineral owners by ensuring that they receive accurate returns for mineral production on their land. Distribution of payments is made twice monthly for revenues collected for leasing and production activities on Indian lands.

In response to feedback from the Indian community, MRM proposed a separate royalty valuation rule for crude oil produced from Indian leases. The new rule, when final, will add more certainty to the valuation of oil produced from Indian lands, eliminate reliance on posted oil prices, and address terms unique to Indian leases. The rule is expected to result in additional Indian oil royalties of approximately $4.7 million.

In Farmington, New Mexico, MMS participates in a Departmental effort, implementing a new concept in serving our Navajo constituents. The Farmington Indian Minerals Office (FIMO) unites employees from the Bureau of Indian Affairs (BIA), Bureau of Land Management (BLM), and MMS, under one director for outreach, inspection, enforcement, and mineral revenue compliance services to industry and American Indian stakeholders. The FIMO office was established as a permanent DOI office on September 28, 2001. In addition, the Department's Indian Minerals Steering Committee, made up of representatives from BIA, BLM, MMS, and the Office of Special Trustee for American Indians (OST), is assessing the feasibility of expanding the program to other geographic areas having a significant population of Indian mineral leases

and lessees.

Minerals Revenue Management Program Challenges

Continuous Improvement

MRM's reengineering initiative has provided a new financial system, a robust data warehouse, and an array of new tools and applications for financial management and mineral revenue compliance. When fully realized, the reengineering initiative will dramatically modernize both the financial and the compliance and asset management business processes and supporting systems. MRM plans to gradually introduce additional enhancements, especially in the area of mineral revenue compliance. As these changes are embraced and applied by the compliance staff, the environment will continue to allow for more and more changes and improvement. This phased approach was anticipated from the outset of the reengineering effort in order to allow for staged implementation as more knowledge is acquired and applied.

These new processes and system enhancements address MRM's continuous improvement objectives for mineral revenue compliance. However, several offsetting factors contribute to the need for an overall increase in operations and support funds during FY2003 to support MRM's new information technology environment

à Robust new tools and capabilities will improve MRM's ability to accomplish its mission and goals but will require ongoing maintenance and support.

à The new systems and tools, coupled with growing requirements for remote access, place an increased demand and a growing dependency on MRM's networks and enterprise systems. This requires continuous upgrades to ensure a stable, secure computing and communication backbone for the new systems.

à Industry is anticipating major cost increases for enterprise software systems (database, operating systems, office automation, etc.) upon which our new systems and networks rely. For the past 5 years, IT professionals' salaries have been increasing at a rate greater than 10% per year in the Denver area. The only way MRM has been able to maintain adequate funding for its primary IT providers is by reducing enhancement work performed on systems scheduled for replacement because of the reengineering effort. The cumulative effect of the increased costs of IT professionals and the implementation of the reengineered system prevent a similar approach in FY 2003.

Expanding RIK Opportunities

The President's November 13, 2001, decision to fill the SPR greatly expands the role of RIK in the Gulf of Mexico (Gulf). When completed in 2005, MMS will have delivered approximately 120 million barrels of crude oil taken in-kind from Federal leases in the Gulf to onshore market centers for utilization by DOE in filling the SPR. There are associated transportation costs and a need to expedite the oil RIK system as a result of the President's decision to fill the SPR. MMS has requested funding for an automated oil RIK system in FY 2003, which will enable the program to handle the added SPR effort. Timing for the implementation of the oil system depends on funding availability.

The SPR RIK initiative at 130,000 barrels/day and the continuation of the Small Refiner Program at some 50,000 barrels/day, will result in much of the Gulf oil production royalties being taken in-kind.

FY 2003 Budgetary Impact

To address these challenges while maintaining our accomplishments, we are requesting $2 million to cover increasing automated systems operations and maintenance costs. Additionally, we are requesting $6.015 million to fund development of the automated infrastructure to support the expanding oil RIK program.

MMS's FY 2003 Budget Request - Highlights

The MMS budget request totals $281 million, a net increase of $21.5 million or slightly more than 8 percent above the 2002 enacted level of $259.5 million. The $21.5 million increase combines program decreases of $14.3 million with $3.6 million for uncontrollable and related cost changes (primarily pay raises and GSA rent increases); $21.8 million for programmatic increases, and $10.4 million for a government-wide legislative proposal to shift to agencies the full cost of the CSRS and the FEHB Program for current CSRS employees. In addition to the programmatic increases described above for the OMM Program (+$13.7 million) and the MRM Program (+$8 million), we are requesting the following decreases:

· a decrease of $0.8 million for the Center for Marine Resources and Environmental Technology which will be eliminated due to higher priorities for oil and gas exploration and extraction; and

· a decrease of $0.8 million for the Marine Minerals Technology Center which will be eliminated due to higher priorities for oil and gas exploration and extraction;

· a decrease of $0.5 million for the Offshore Technology Research Center that will have funding reduced due to higher priorities for oil and gas exploration and extraction;

· a decrease of $3.0 million for the Royalty Legacy System, which was replaced by the reengineered system in FY 2002;

· a decrease of $2.2 million for the Environmental Studies Program that will allow for the continuation of existing projects and starts for limited but critical new projects;

· a decrease of $1 million in the Pacific OCS Regional office from a review of its operations; and

· a decrease of $6.0 million for the completed gas management system acquired in FY 2002 in support of continuing RIK pilots and longer-term projects.

Revenue Sources

FY 2003 Proposed Operating Appropriations/Offsetting Collections

dollars in thousands	
Royalty and Offshore Minerals Management	$174,640
Offsetting Collections	$100,230
Oil Spill Research	$6,105
Total	**$280,975**

The MMS receives funding for operations from three sources: the Royalty and Offshore Minerals

Management (ROMM) appropriation, Oil Spill Research (OSR) appropriation, and offsetting collections (primarily from rental receipts from offshore leases). Since 1994, when MMS received authority to retain a portion of OCS rental receipts (offsetting collections) the share of the agency funded with appropriated funds has decreased substantially. The share of MMS's total budget funded from offsetting collections peaked in FY 2000 at 52 percent. In FY 2003, approximately 37 percent of MMS's funding is proposed to come from offsetting collections.

Several years ago, dramatic increases in leasing activity in the GOM made it possible to shift a larger portion of MMS funding from direct appropriations to offsetting collections. The increased GOM activity was made possible by new technologies that allowed exploration and development in very deep water. Examples of these new technologies included the rapid expansion in the availability of high quality 3-dimensional seismic data, inexpensive geo-science workstations, and seismic processing advances that allowed geo-scientists to look below the previously impenetrable layers of salt. In addition to the technological advances, Congress enacted legislation (Deep Water Royalty Relief Act of 1995) that has encouraged deepwater exploration and production.

The combination of very favorable geologic characteristics, technological advances, and economic incentives caused leasing in the GOM to increase almost ten-fold between 1992 and 1997. In 1998, however, the number of tracts leased in the two GOM sales declined by 37 percent from the record levels of 1997. While 1998 marked the first time that the number of tracts leased in the GOM had declined in the past several years, the number of total active tracts actually increased in 1998 by over 12 percent. In 1999, the number of new tracts leased (333) fell 71 percent below the 1998 level and 81 percent below the peak level reached in 1997. In FY 2000, the number of tracts leased (553) in the GOM increased by almost 70 percent over FY 1999. In FY 2001, the number of tracts leased grew again as 753 new leases were issued.

While FY 2000 and FY 2001 saw the number of tracts leased increase, MMS does not expect new leasing activity to return to the FY 1996 - 1998 level in the near future. Because of this lower level of new leasing activity, MMS is requesting the cap on currently authorized offsetting collections be lowered to $100.230 million in FY 2003.

In addition to appropriations for operations, MMS receives appropriations for distribution of the states' share of onshore mineral receipts. In FY 2003, MMS estimates that the states' share of these onshore mineral receipts will be approximately $674 million. This amount is slightly more than our FY 2002 estimate of $670 million.

FY 2003 Proposed Permanent Appropriations

(dollars in thousands)

Mineral Leasing Associated Payments *(MLAP)* 669,880

National Forest Fund Payments to States *(Forest Fund)* 3,475

Payments to States from Lands Acquired for Flood Control, 951

Navigation, and Allied Purposes

(Flood Control)

Total $674,306

Conclusion

Mr. Chairman, that concludes my written testimony. At this time I would be happy to answer any questions you or other Members of the Subcommittee may have regarding any aspect of our budget request for FY 2003.

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